

COMMISSIONER LEWIS: Thank you very much for your presentations.

Dick D'Amato.

COMMISSIONER D'AMATO: Yes. I'd like to get an opportunity to go further with your analysis. Thank you for your testimony, all of you on the panel. I'd like to focus on the last --

COMMISSIONER BECKER: Could you speak a little louder for me over here?

COMMISSIONER D'AMATO: Maybe I should put my microphone on. Does that help?

I asked a question of the Boeing representative. Of course, he's only got a certain limitation in his ability to answer because of his corporate responsibilities. But the question I had was based on the problem I have with the Chinese inability to conform to a rules-based system that is a Western oriented system. And maybe it's too much to ask them to do that. But the question is, if we are going to put pressure on the Chinese to conform to a fair system of free trade, is it going to be harder for us to do so within the context of the WTO than it is now in a unilateral way with unilateral leverage?

COMMISSIONER LEWIS: Is this an open question to all three?

COMMISSIONER D'AMATO: This is a question to Don, but I'd like the others to also answer it if they can, because I think it's absolutely critical for us to understand whether we're going backwards or forwards in our ability to open the Chinese market to free trade with this WTO initiative we just had last night.

MR. HELLMANN: That's a very big and very good question. My answer is that admission to the WTO at least removes the debate about China from the annual Most Favored Nation discussion in Congress, which I think was a distraction because it was an annual introspective hour on an array of issues, some of them having nothing to do with trade and some of them having a lot to do with trade. So the WTO at least gets rid of that or will not diminish that.

The second part of it, however, is the bad news. Joining the WTO, as I indicated in my testimony, is just the second phase. The question is whether it is an effective arena within which to bring the Chinese into compliance with rules-based behavior is a very debatable one. I asked this of a former ambassador to China in Washington, and he was very much in favor of the WTO admission. And his answer was the WTO was a kind of toilet training manual in free trade, designed for the Chinese. And I challenged him on this because

I said it's 23,000 pages long, it takes four linemen to carry it. Most toilet training manuals are a little shorter and to the point. But the anecdote makes my point. I have my own serious doubts that the WTO is the vehicle, in its current form, the right vehicle to do this. I have other questions about the WTO, but that's another matter. And so the answer is I don't know whether a mechanism can be devised to truly bring the Chinese into compliance with rules based things. But an effort should be made to create one, and the current form of the WTO is a clumsy, awkward venue, and I support their admission, but I have grave doubts.

COMMISSIONER D'AMATO: Can we ask the other panelists to comment. And before that, I would like, Don, if you have any ideas, further ideas about what recommendations you would have in terms of what you just mentioned, in terms of addition -- a different kind of mechanism that would be more effective, I would certainly be interested in getting that.

MR. ECKES: I think the question you raise is an excellent one. Several years ago I sat down with a group of our former trade negotiators who had been involved in the GATT process from the 1940s. That tape will be part of a book that's coming out next year. These negotiators observed that there was often an enormous gap between the rights and obligations of new

members to the GATT system. Countries customarily cut off far more than they could chew, and there was often a long period of implementation in which the asymmetries only got worse.

I would anticipate that this would occur in the case of China. If any of you think the China agreement is going to reduce the U.S. trade deficit over the next five or 10 years, I would strongly disagree with you. As China complies with the terms of the GATT or of the WTO mechanism, if it does, we may have a problem similar to the one we had with Japan after it joined GATT. I don't know. I'm skeptical of any agreement that's written according to a political timetable. And I regret that this current agreement seems to have been driven by a political timetable, rather than by the realities of careful negotiation. It is my understanding that in the NAFTA and Uruguay Round negotiations, the details were actually negotiated after the principals proclaimed publicly their agreement.

COMMISSIONER LEWIS: Thank you.

MR. CUTLER: Our position seems to be pretty clear in this area that WTO for China will certainly be a good first step. It may not answer all the questions, but we've been talking about this thing for I don't know how many years. Are we going to get

them in, and if so, maybe we can work together to accomplish a lot of the problems that we've had in this area. Now it seems like it's not even 24 hours later and we're already starting to talk about, "Well, it's not going to go far enough. It's not going to do enough. Or we should have stronger provisions and regulations and stipulations in WTO." I think our position in the auto parts industry is it's a good first step. Is it going to be the only step? Pretty clear, no. But let's see what we can do to work with what we have.

COMMISSIONER LEWIS: George.

COMMISSIONER BECKER: I didn't know if I was next.

COMMISSIONER LEWIS: Murray's next.

COMMISSIONER BECKER: No. No. You're going to China, buddy.

CHAIRMAN WEIDENBAUM: I'd like to ask Mr. Cutler a question relating to his three recommendations at the end of his statement. The first and the third deal with eliminating trade barriers and anti-competitive practices. I welcome that. It's the third one -- the second one I have the problems with. But two out of three, that's not bad. Better than most recommendations that I get.

But the second one is one I seriously have trouble with. You advocate setting, "Specific deficit reduction goals for countries with which the U.S. has substantial bilateral trade imbalances."

I worry that focusing on bilateral balancing puts trade in a straitjacket, and here's the kind of anomaly I come up with. Australia regularly runs a trade deficit with the U.S. Year-in, year-out we export far more to the Aussies than we buy. So, to be fair, to be consistent, if we follow your approach, we're going to have to reduce that substantial bilateral trade imbalance with Australia. Is that part of your recommendation?

MR. CUTLER: In our case, of course, we're talking about auto parts, and we're talking about auto parts specifically with Japan or Japanese controlled other countries. Asian areas, primarily.

CHAIRMAN WEIDENBAUM: These are written as fairly general statements.

MR. CUTLER: The interpretation would be auto parts in Japan. That's the authorization we have from the Department of Commerce, the U.S. auto parts industry. Our concern is in this area that we get close in some of the previous regulations and agreements with our Japanese counterparts, but we never can seem to get a defined number of how we will work

these things out. Even though in the last agreement -- and by the way, the current agreement expires at the end of next year, and that's what's going on right now is us building up to a new agreement. Our biggest problem has been that even though we thought we had gotten some very clear numerical agreements in the previous agreement, our partners who negotiated it with us, the Japanese, never made any public statements that they would live up to those numbers.

COMMISSIONER LEWIS: What you're saying, Ron, is that all three of your recommendations are limited to auto parts?

MR. CUTLER: That is correct.

COMMISSIONER LEWIS: Okay.

CHAIRMAN WEIDENBAUM: That's not what you say in your statement.

MR. CUTLER: Well, our interpretation should have been clearer then. We're talking about auto parts. That's where our group, the U.S. Auto Parts Advisory Committee comes from. Auto parts.

CHAIRMAN WEIDENBAUM: Okay. Thank you.

COMMISSIONER LEWIS: Thank you very much.

COMMISSIONER WESSEL: Can I just follow up on the same line?

COMMISSIONER LEWIS: Yes.

COMMISSIONER WESSEL: I believe it was Cy Vance and Henry Kissinger in 1985 who wrote an article looking at the intractability of the U.S.-Japan trade issue, that perhaps some measurable targets for deficit reduction were worth while, that at that point it would be in the -- in Japan's hands as to whether they wanted to import more or whether they wanted to export less. Yesterday we heard from Intel in the semiconductor industry who indicated that the success they had achieved was because of measurable targets. I believe it was a 20 percent market share as part of the semiconductor agreement.

COMMISSIONER LEWIS: That was the target, but they're doing more than that.

COMMISSIONER WESSEL: They're doing much better. And they in fact were not trying to increase their market share, not trying to define what it would be, but rather a floor.

COMMISSIONER LEWIS: Right.

COMMISSIONER WESSEL: In terms of auto parts, as well as the overall auto industry, we've seen a problem with getting the dealership agreement adhered to, and many of the others. When the agreement comes up next year, are you going to be seeking specific targets or are you going to be seeking to change that agreement, and how effective do you think that will be

in light of the current politics and situation in Japan?

MR. CUTLER: We're very familiar with the Intel situation and wish that we could follow in their footsteps because they've been very successful, had very good negotiating skills in pulling that off, and yes, we will not give up in that area because we think it's a very good way to try to move forward. So we will definitely try to build that into the post-2000 agreement with Japan. Problems will be that we came very close to achieving this thing at the last agreement. In fact, the U.S. side came out very clear that there were clearly numerical numbers that we could drive through, but we never got the Japanese counterparts to agree to those numbers. And if we cannot --in our opinion it's a very key point -- if we cannot get some kind of numerical number to use as a report card, everything else starts to sort of fall apart because -- and there's all kinds of other reasons why they couldn't do this or why they couldn't do that.

COMMISSIONER LEWIS: George.

COMMISSIONER BECKER: At least two of you -
- I think maybe three -- referred to a level playing field. And this is something that always disturbs me very much.

But in talking about a level playing field, this is a very amazing thing to me. Mr. Hellmann, in one of your comments, if I understood it right absent written testimony, you talked about the societal way of doing business. I'm going to say it was back in the '70s when I went to China, shortly after relations were normalized, after we opened an Embassy. I was there when they were actually moving into the embassy. I went to a steel mill in Beijing. Capital Steel was the name of it at the time. It had two antiquated '50s blast or DOFs, and they had two Russian blast furnaces that were antiquated also. They employed 60,000 people in that mill that we would have said would have employed maybe 3,500 or 4,000 people. The object was clearly to provide jobs. You didn't even know how in the hell they kept track of it. But I witnessed the same thing in Poland in steel mill after steel mill in which they had 28 -- 35,000 people, and they were in mills that we would have had anywhere from 1,500 to 2,000 people in on a capacity size.

But the reason these societies couldn't get rid of these people was because they had no safety net.

Somehow or another they had to provide income. They never even had ways of gauging how much to pay them. They got paid on the basis of family size and longevity and employer connections, and whether they showed up

for work or not many times was immaterial in the whole process of this.

The long and short of this is they have to provide jobs one way or another. Making a profit is secondary to that. And a lot of that still exists today. They won't switch from the old antiquated blast furnaces because it would reduce the number of people, and so they continue to pollute. This is true in Russia and it's true all through the Eastern European countries because they have to provide jobs within this whole process.

I feel that in dealing with these countries, most times these trade agreements are used as weapons against the workers here in the United States. For us to be able to compete on whatever pricing mechanism they send, workers are pushed and coerced into giving up wages and benefits in order to be able to compete. Communities are asked to stretch subsidies in ways to provide infrastructure and other things and make the companies competitive. In the final analysis, they have the decision either to close down after so many years of dealing with this or move offshore and settle.

So when you talk about a level playing field, it really disturbs me, because I don't see how we can reach that. And my question to you, is there a

way out of this morass, as you see it? Do you three gentlemen see any of this in your business relationships? Do you feel that to have a level playing field, they've got to come on our side of this, or do we have to go on their side? Which way do you see this going?

COMMISSIONER LEWIS: George, this is addressed to all three? George?

COMMISSIONER BECKER: Any of them. They all talk about a level playing field.

MR. CUTLER: Let me give you just a -- let me tell you my first reaction to this. The U.S. auto parts industry, we've been trying to do this for the last 25 years. That's about as long as U.S. and Japan auto issues have been going on. Let me give you two good examples of how off balance this playing field is in the U.S. auto parts industry.

If a U.S. auto parts company wants to do business with a Japanese manufacturer, he has to figure it some way to get through what we call the karetsu relationship, which means a U.S. or, excuse me, a Japanese supplier that is tied to a Japanese manufacturer from an equity ownership or controlled situation. Very, very difficult for him to do that.

Second example is a U.S. after market parts supplier trying to get business in Japan has to get

through this whole safety regulation procedure. The Japanese government puts safety procedures on each of their key safety related items. And it's almost impossible for a U.S. parts manufacturer to get through this regulation procedure. Only two in the last four or five years. So for all practical purposes, the after market in Japan is blocked out for U.S. manufacturers.

We have to have a very good specific tied to numerical numbers -- we believe, the U.S. auto parts, trade agreement with Japan that will help break down these barriers and start to create some kind of a level playing field. We let them come into this country, and they can operate with virtually no barriers at all, nothing even close to the barriers that U.S. auto parts people have to put up with in Japan.

So the key here to us again is we have to have a very specific trade policy that knocks down these barriers.

COMMISSIONER BECKER: Let me make sure that you understand what I'm looking for. To reach a level playing field, you could reach it several ways. We could get rid of our clean air laws, our clean water laws, our minimum wage, our Social Security, our Medicare. We could do a lot of things in the United

States in order to lower this, right? Or we could drag them up. Which way is this going? How do you see this in your history, from your end, Mr. Eckes and Mr. Hellmann? How do you see this evolving? Where are we headed as a nation?

MR. HELLMANN: First of all, your question is a good one. It's extremely difficult to answer. No one's going to win. You're not going to get environmental control laws in China because people jump and down in the streets of Seattle on behalf of clean air, or rules are imposed on American manufacturers that lower their profits to be in compliance. I would support all that stuff, but you're not going to in China -- unless you find an alternative to coal, for example, how are you going to stop air pollution with 1.3 billion people? That's not going to happen soon in China, at least not in 40, 50 years. You can work on it. How are you going to deal with poverty and these non-economic issues that you're discussing now? Human rights and whatever are relevant both to the culture, to the level of development, as well as the policies of the government.

All we can hope for, other than asking these abstract questions about whether we can do this, is that we understand the limitations, we understand what the karetsu's are, and how to deal with them.

Pardon me, to give you an illustration which goes back to your earlier panel this morning. One of my assistants from the university worked in the Special Trade Representative office because he was selected as an outstanding young leader. He walked into the Special Trade Representative's Office about four years ago, and they were just in the middle of negotiating a general agreement with Japan. He was very intimidated because all of the great and powerful associated with that office were there, so he hid behind a palm. Finally, someone asked, "What is a karetsu? Who knows anything about it? We're about to negotiate." And he sat there behind the palm. And finally he got out and raised his hand and said, "I know about it." He happens to be married to a Japanese. He's fluent in Japanese. Has an advanced degree in it. He said, "You're our man." And he became immediately, out of this recruitment process.

Now, this goes back to your question. You have to start with a framework of understanding in these areas, of which this country is replete. And you have to do this, I think, from the top down. There is no answer to your question. The playing fields in China are not going to be level with ours for a long time. And the challenge is to negotiate an acceptable set of arrangements on a whole host of levels, from

security to environment. You're not going to establish standards and regulations, except in very selected areas. It's going to be a continuing and ongoing process. We obviously have to stake out our claims and defend them intelligently and aggressively, but we have to understand that they're probably not going to be in compliance with what we have. What you do about that, I don't know in an abstract philosophical sense.

COMMISSIONER LEWIS: Mr. Eckes.

MR. ECKES: A quick response. Until the dollar collapses -- and I'm not predicting it tomorrow or the next day -- I doubt we as a nation are prepared to pay the price to achieve a level playing field or to remove the trade deficit. We as a nation have a broad multiplicity of interests, and I don't think our leadership is prepared to put access to foreign markets ahead of nuclear arms agreements and other policy considerations. I wish I could be more optimistic in regard to the question you've raised, but I can't be.

COMMISSIONER LEWIS: Michael, you've already gone. Let Dimitri go now.

COMMISSIONER PAPADIMITRIOU: Thank you, Mr. Chairman. My question is actually for the two individuals that represent the universities, the academics, I guess, on the panel. And that's Professor Hellmann and Professor Eckes.

You have indicated, Professor Hellmann, that in the previous hearings that we have held, the issue of the trade deficit was actually not appropriately placed in terms of the causes and consequences. And I wonder whether you could tell us what should have been the question -- how should the issue have been raised? Clearly, one of the major interests that we have is solving the trade deficit, if in fact the trade deficit is a problem. And whether recognizing that \$320 billion projected trade deficit for this year can be sustained and if, it is to continue, and for how long can it be sustained, and whether the solution to that is really a matter of savings. So my question to you is do you see anything different other than what we have been told?

And I guess I would ask the same question of Professor Eckes. Since he is a historian he has seen this, perhaps deja vu for him, not at the level that it is now; Professor Eckes do you see that the problem with the trade deficit is really the flip side of the identity equation which has to do with investment and savings and -- whether it's government savings or private savings. Thank you.

MR. HELLMANN: Well, first of all, what was said in previous testimony regarding the causes of the trade deficit is quite true. I mean, if countries

don't save and others do save and process gets going, that's what happens. And you're going to be stuck with a trade deficit. Furthermore, the odds are very high in the foreseeable future that the patterns of consumption in the United States and the patterns of saving in Asia are going to continue. Furthermore, it's very likely that the aggressive growth of Asian economies, now that this financial crisis is over, is going to be back on track again.

So my answer to you is the deficit not only will be with you, it will be with you in spades.

COMMISSIONER LEWIS: You mean it will get worse?

MR. HELLMANN: It will probably continue to grow. Whether that's good or bad or -- in one economic sense, is irrelevant. As long as it works. That's what an economist would say. My point and I'll summarize it very briefly, is threefold. I mean, first of all, the aggregate size of both the deficit and of Asia is going to become so substantial in the next decade or two that the question really is how do you adjust to it.

Mr. Waldmann, I've been on many panels with Ray before. Boeing has bet the store on China. I mean, 60 percent -- at one point it was 80 percent of commercial planes to be sold in 1995 were to suppose to

go to China. You better pay attention to what's going on in China, I'm telling you, if you've bet the entire company on that account. Now, they scaled these back because of the financial crisis, not that much.

But my first point to you is the size of Asia, its aggregate size relative to demand, is so great and so important it deserves special and privileged treatment in a variety of ways, especially because -- which is my second point, which is they are going to continue to operate by different rules. One of the most startling things in the second half of the 20th century, I would argue, second only to the Cold War, is the emergence of Asia, and particularly Northeast Asia, into the center of the global political economy. Under a development model which varies from country to country but is quite different from democratic capitalism as we know it, and that's not going to change.

A quick illustration. After World War II we occupied Japan, created an anti-trust division in administrative justice, broke up the Zibatsu, created an international environment so that 40 years later they had a nominal per capita GDP 30 percent greater than we did. Is there anybody in this room and on this Commission that believes that Japan is a democratic capitalist country like the United States? If not,

then why did the IMF think they could go into Korea by getting a little transparency in the financial services area, getting the banking, the interest rates in a certain line. They could do there what we did not do in 50 years in Japan. That's not wrong, it's preposterous. That's what I mean by asking the wrong question.

Of course, it's good to be transparent. And Koreans benefited enormously. But to suggest that somehow this is going to lead to a convergence of Asian behavior and our behavior, or that the nationalism behind all this is going to dissolve because institutions and politics are as important, and culture, are as important to understanding both the origins of the trade deficit and, above all, the remedies that are doing. The economic analysis is correct. But it does not focus on the central concerns of these societies and, from my point of view, what ought to be a concern of this society. These questions are different.

COMMISSIONER PAPADIMITRIOU: But we certainly cannot change their society, can we?

MR. HELLMANN: You can't change it, but there's this crazy book written by a Harvard professor called Clashes of Civilizations which said because you couldn't change things, you're going to be in a state

of adversarial conflict with them. I mean, if I believed that I guess I'd retreat into the mountains. You try to create civilizations and create institutions to mediate differences between different societies. And what we're talking about is creating an operational arrangement that allows those adjustments to occur, even though these differences exist. That's what civilization is about. We've got a challenge now that we've never had before.

And particularly if you have a hearing dealing with Asia, I felt, at least from my point of view, my obligation was to point out that there are these fundamental differences which are not generally noted because everybody wants to create universal norms and regulations that apply, and that these have to be factored into any solutions that you have, even though you're going to be frustrated by not reaching.

MR. ECKES: I find myself in general agreement. Let me supplement with a couple different comments. I have difficulty reducing the trade deficit problem to a simple equation, as many economists are prone to do, because I don't think that equation tells us a lot about the causation, and it may not reflect adequately certain non-economic factors that are not included in the variables.

Is the trade deficit going to be a problem for American workers in import competing firms? I think it's going to be and it will be accentuated to the extent we try to produce in the open American market with commodity labor. For consumers, we know the many benefits.

The issue that you have to be concerned about -- and I'm sure you've given consideration in your other hearings -- is whether foreign people and governments are prepared to continue accumulating dollars around the world for a long time to come. Will the euro become a substitute for the dollar. A new Asian currency could emerge in another 30 years. Recall that the dollar crisis of the early 1970s prompted the Europeans to devise plans for a common currency. It took them 25 or 30 years to effect it. At what point are people going to prefer other convertible currencies to dollars? At that point the trade deficit becomes a financial problem. It may require higher interest rates in the United States in order to persuade investors to hold dollars.

COMMISSIONER LEWIS: We're going to have questions from Dick and then from Murray, but I want to ask a question first. Is the trade deficit a problem for the United States? We've heard varying opinions on

that. What is your opinion? Is the trade deficit a problem? And if it's a problem, what is the problem?

MR. ECKES: Obviously, it's a problem for import-sensitive workers. It may be a particular problem for those with sub-average IQs, and presumably half of Americans have them, who can't learn higher mathematics and computer skills. Fortunately, all of us in this room are past that threshold, but it's a problem for substantial segments of our population. And I see pockets of them in Appalachia, where I'm resident, and we see them in our inner cities. I'm very much worried about the problems low-skilled Americans may have competing with cheap foreign labor in a global marketplace.

Is it a problem for the nation over the long run? Obviously, in the short run for the time being, the dollar seems to enjoy wide acceptance. At what point are people going to prefer to hold other currencies because they have questions about the quality of the American currency?

At some future date I think the trade deficit becomes a major problem. As I read history, great nations do not run perpetual trade deficits. They may run them for short periods of time, but not perpetual deficits. As you know, our deficit has continued for nearly 30 years. I don't see anything on

the horizon that's going to reverse it, such as World War I did.

COMMISSIONER LEWIS: We'll, we were told that the deficits are good because it's foreigners that are really financing our investment and consumption.

MR. ECKES: There is a positive side to foreign investment, but I think those who say we can ignore the deficit are mistaken.

MR. HELLMANN: On one level, obviously, not just a short term existential one, the trade deficit is not intrinsically bad. The economists are right. As long as it works. Where they're wrong, in my opinion, are in two areas. One is to fail to appreciate how integral this whole process is to political decisions.

This is an abstract metalanguage. They create a world in which all of this works. But the fact is that the current world works as it is for decisions, just like this Commission I mentioned earlier. You've got a trade deficit spurt now because we've agreed that the catastrophe of an Asian financial collapse would be worse than having a trade deficit. Now, that's not just the market working. That is a correct decision made by people to avoid this bump in the world, because they were sailing on uncharted seas. And I think that trade deficit is contingent. It is contingent on political decisions internationally and can be mediated

by international institutions. And it's absolutely essential that you do that for the second reason why a trade deficit is awkward and bad. Because if there is a shift in productivity -- if the law of comparative advantage works -- people are going to be dislocated. People are going to be upset. I mean, people are going to lose their jobs.

Now, if you treat labor as a commodity and you say it's totally mobile, you don't worry about it. Let the people figure out what to do. But obviously most societies don't do that, or you shouldn't do that.

And therefore, it strikes me that the trade deficit has sectoral impact which can be devastating, and this is why I mentioned the FEMA issue. You don't have to have an industrial policy, which is the way this is usually kicked around in Washington. What you could have and probably should have is some mechanism to respond to severe dislocation of workers -- if Jesse Helms and others allow the Chinese to suddenly drop all restrictions on textiles by whatever it is, January 1, 2005, the impact on people who manufacture textiles is quite clearly going to be devastating because the Chinese have the capacity to supply the world with textiles at a very cheap rate. Now, that doesn't mean you should prevent them from doing so, but it sure means you have an obligation to the people that live in

the United States to adjust to that. How you do that, whether you do it, whether you should let the market decide or not. I happen to think probably you should soften the market by doing something constructive, and I just don't see those questions, to go back to your thing, being asked in that.

COMMISSIONER LEWIS: Thank you. Dick.

COMMISSIONER D'AMATO: Yes. I just need to take it one step further. As the Chinese economy recovers and other Asian economies recover, we've heard that there may be a lack of -- less of a willingness on the part of investors in those countries to continue to fund our trade deficit at the current level. Maybe they will put more of their funds back into their own economies, which would put pressure on the dollar in our own markets. And I'd like you to address the question of how vulnerable do you think that will leave us.

But the more important question I have for you is what is in the mind of the Chinese in terms of these deficits, do you think, as they grow and as the Chinese hold more and more dollars? Do you think --

COMMISSIONER LEWIS: Or treasuries. Government certificates.

COMMISSIONER D'AMATO: Or whatever. Yes. Claims on our market. On our economy. To what extent

do you think the Chinese are prepared or will be prepared, willing to use threats or intimidation, to get their way on other issues of importance to them, economically or politically, as we become more vulnerable to their leverage as a result of their holdings of dollars and certificates?

When we had that agreement with Japan a few years ago in the auto parts area, we did a lot of work in the Senate on that, our understanding was when Mr. Kantor got into the final room to make the negotiation that, instead of coming out with a pie, he came out with a muffin. And that was because there was a threat that if we pushed the Japanese too hard that they would have gone in and withheld buying our treasuries. I don't know how true, that rumor was rampant in Washington at the time. That was sort of a fly in the wind, an indication of what we might expect on the side of the Chinese in this area.

So I'd like -- do you think we have to worry about this kind of behavior on the part of the Chinese in the medium run?

MR. HELLMANN: Two responses. One is how vulnerable are we to Asia's withdrawing money. There was a point a few years back where the Japanese did own a significant number of T-bills, but that period, as far as I know, is passed. At least it's not as great

as it was then. That remains money is the most fungible substance.

I would put it a little differently, money is the most fungible substance in the world, and the fluctuation is not just in terms of its impact on our disability of our economy, but the impact of what you're seeing in the Asian financial crisis, which impacted us almost indirectly because of actions of speculators or whatever. That's really serious. Something has to be done about the international financial system. To minimize the potentially disruptive effects that the age of the computer and derivatives and this whole business has done. And we've kind of gone away from addressing that.

But I guess my immediate reaction is that there is always the possibility that they will reinvest in Asia. It's unlikely in the short run. They're over invested. They have excess capacity now. They're unlikely to do that.

As far as threats and intimidation go, I'm trained in politics as well as economics, and my reaction is that a holistic approach to dealing with China and Japan for that matter is required. For the life of me I don't understand why we have not leveraged our overall political military position in that region to address the more narrow issues of economics. I

mean, we're willing to do, someone was saying earlier, embargoes, and how punitive they may be. Well, the flip side of this, I think it was an anomaly of the Cold War that economics and politics were separated. That was because of the peculiar structure of the Cold War itself. In the real world they're never separated.

And that they shouldn't be linked to deal with maximizing our overall interests. Rather than forcing people in specific industries to try to bargain with countries or industrial. It strikes me as being just plain bizarre. I mean, I don't understand it.

I've spent my life studying Japan, and I've never really understood why we underwrote the security of Japan, prevented them from having even a change in political regime for 45 years because once the Cold War ended it was chaos over there, and never once used the leverage that we were paying for -- I just don't get it. Same with China. China understands that our presence in Asia assures the kind of stability that allows them to prosper. That should be on the bargaining table if you're arguing about economic issues. Why it isn't is an absence of a coherent strategy beyond the Cold War mentality, and an absence of what we said earlier, of leadership that says that you better set out and do this.

COMMISSIONER LEWIS: You just said something that Mr. Waldmann also earlier said, that you have American companies negotiating with foreign countries.

MR. HELLMANN: That's right.

COMMISSIONER LEWIS: Isn't there an inherent inequality in that -- the negotiations?

MR. HELLMANN: Of course.

MR. ECKES: Which way?

COMMISSIONER LEWIS: Well, they can set rules that the companies can't fulfill.

MR. HELLMANN: No, I agree.

COMMISSIONER LEWIS: Mr. Weidenbaum.

CHAIRMAN WEIDENBAUM: Mr. Cutler, I'd like to get back to the auto parts situation. And I -- here's where I'm coming from. In tours in both the Treasury and the White House I interacted with lots of foreign government officials, and I learned the hard way, if I just presented problems that the U.S. faces because of the obstacles that they put in our path, be prepared to hear the other side. They'll cite you chapter and verse on the obstacles that we put in their path.

So, in the case of auto parts, when I heard your presentation on the problems that American companies face in China and other countries, it

resonated. I saw a check mark. I believe that's totally correct. On the other hand, when I'm just reading newspapers in the United States in recent weeks, I find that our courts are punishing severely companies -- insurance companies -- who buy auto parts from other than the OEMs. So, you know, our hands are not that clean either. Are we holding them to a higher standard than we're holding ourselves?

MR. CUTLER: Well, relating to the question that had to do with this recent court case on after market parts, I think that primarily dealt with people feeling that they were getting equal to the original equipment part and it had been proven, in many cases, they -- they had not been getting that. And that's a separate problem. But we're very familiar, since almost every positive statement we've made about our problems in the auto parts industry, you are absolutely correct. The Japanese people have a one-to-one basis.

For everything we can bring up, they also have an excuse of why they can't do it. The last two to three years it's basically been, "Please don't be too hard on us because we have an economic problem here. We're suffering and you shouldn't be difficult and hard on us." So we're very familiar with the situation of dealing with the Japanese.

That's why we'd like to insist again, do the best job we can to get a numerical rating score in this agreement so that we can measure them on productivity and improve it. You take this level playing field that we've talked about. We feel that we're at the bottom of the 10-yard line, if you want to use a football field as a comparison, and that's probably a pretty good way to do it. And they're on -- about our 10-yard line trying to get the ball in. If we can move our ball up to the 20 or 30-yard line, I think we would be very, very glad that we've made some significant improvement. We'll want to move that ball a little bit forward.

COMMISSIONER LEWIS: Does anybody else have a response that they want to add to that?

CHAIRMAN WEIDENBAUM: Well, let me say I hear you. I still have this problem. It's a very practical one for any government official who deals with the officials of other governments. If we only recognize their shortcomings and we ignore our shortcomings, and their -- I'm not plugging my book, but in my unnamed text book all six editions have long lists of U.S. barriers to the exports from other countries. I assure you these other countries are well aware of that information. And unless we indicate that we're going to do something constructive to reduce our

barriers to their exports, we come across as, to put it crudely, rather hypocritical. That's my concern.

MR. CUTLER: Well, I think we're listening to your concern and understand your concern. In the area specifically of auto parts, though, the barriers are not level at all. If you compared the barriers that the Japanese governments have on auto parts versus the barriers that we have on auto parts, you'll find that there's a drastically different set of circumstances.

CHAIRMAN WEIDENBAUM: I appreciate that, Mr. Cutler, but to state the obvious, this is not the Congressional Commission on Auto Parts. We have a broader mandate.

MR. CUTLER: I understand that. But I think you asked me to come here today to tell you about what the problems are in trade barriers for auto parts. And that's what I'm trying to do. I understand it's only a part of the bigger picture. But our job here today was to try to give you a snapshot in time of problems we're facing in the U.S. auto parts industry, trade barriers with the Japanese.

CHAIRMAN WEIDENBAUM: In days of hearings, I'm -- I have yet to hear any witness -- this is the third day of hearings around the country -- saying -- say, "Here's some barriers that we have to foreigners.

To be fair, to be credible, we ought to get rid of them." I haven't had any volunteer yet.

COMMISSIONER BECKER: Absolutely not.

COMMISSIONER LEWIS: That's not our mandate.

COMMISSIONER BECKER: You sure as hell aren't going to get one. Not here at this table today.

I have sat in briefings, and I've tried to share this in my own way, maybe very inadequately with you gentlemen, and probed some questions with you, because you focused on a level playing field, and this bothers me because I don't think there's a level playing field and I don't see it achievable under the circumstances, and I wanted your ideas. I talked about the difficulties of doing business in the United States. Our nation is on record, at least at the FTAA meetings, about harmonizing standards. And I've raised questions about harmonizing standards, which gets exactly to what Murray is talking about. A lot of businesses visualize that self-imposed impediments in trade in the United States are the social laws that we put on the books, like Clean Air and Clean Water, other aspects of the environment, OSHA, for the protection of workers. This is an impediment to trade if you're talking about business.

So the question is are we leveling standards up or are we leveling standards down. And when Mr. Hellmann talks about us reaching a level playing field, I want to know what the hell we're talking about on reaching a level playing field. Are we going to reach that by stripping away the very sound protections? They say we can't afford Social Security anymore because it's too high. That's an impediment to trade. Business pays both aspects. They pay the workers' share, they pay their own share of Social Security. Medicare could be viewed as a self-imposed impediment to trade. So what are we talking about with this? And I want to know how you feel about this.

Murray, I think that if the citizens of the United States understood that certain trade negotiators were talking about harmonizing standards to where they equalize them, they would be appalled by that. And I don't think this is the way the population is viewing this. And I hope this is not the way, as business people, you're viewing this. That's a statement in response to Murray's statement.

MR. ECKES: Let me make a response. It won't be sufficient, but let me try.

From my vantage point, the prospect of harmonizing standards throughout the world, labor standards, environmental standards, may be a desirable

goal. But practically, it's not one that's going to be achieved in my lifetime or perhaps of anybody in this room. So where we have odious practices abroad that impact the U.S. we may have to rely on what some lawyers would call interface mechanisms. Countervailing and anti-dumping laws are examples of that where you find that they're selling below cost or they're dumping subsidized products. I helped administer those for a while.

We have other laws on our books dealing with child labor, prison made goods, and I think we may disagree about how well some of those laws are, in fact, being enforced in the United States. But we have it within our power, if we choose to exercise it, to enact laws forbidding the importation of certain goods into the United States. Yes, these actions may be in violation of our WTO commitments.

COMMISSIONER LEWIS: Thank you very much.
Michael.

COMMISSIONER WESSEL: Thank you. I find myself somewhat going down a walk down memory lane as we talk about all the trade agreements, many of which Dick and I worked on for 20 or so years in Congress. And it reminds me of what President Reagan said with regard to arms control agreements in the '80s. I think we have to look at trade agreements in the '90s as

living by his adage that we have to trust but verify, and therefore, need to find greater enforcement mechanisms, greater standards by which we measure adherence to those agreements, and effective mechanisms for compliance. And as I asked the previous panel, I'd also ask this panel to, after the hearing, give us their ideas as to what would be effective monitoring, enforcement and compliance mechanisms that this Commission should look at.

It's not our job to negotiate agreements and deal with the counterbalancing issues of what are our barriers, whether we have a budget deficit, whether our companies are competitive, but rather the goal, I think, of the politicians in the United States. And we're not politicians, I expect, in the capacity we serve now.

The politicians, is -- their desire is to raise national income and create jobs and wealth. And that means, many times, trying to fuel our exports. I'd like to ask, though, a specific question of Mr. Cutler.

I apologize for having been out of the room for a short period of time. With regard to auto parts, looking at China. I believe it was in the last few years that General Motors signed a deal to move to

China -- move the facility to China. Create a facility there.

As part of that, the facility was supposed to become self-sufficient, as I recall, in terms of auto parts in the surrounding area in terms of performance requirements, and that close to a billion dollars of technology was transferred by the company to the Chinese to help them essentially create an auto manufacturing -- the capability in auto manufacturing as well as in parts production.

How do you view that impacting domestically here? Is that, because of the size of the Chinese market simply going to enhance their ability to serve their own consumers, or do you view that as a threat of parts coming here in the U.S.? And what's the current history on that?

MR. CUTLER: The situation with General Motors is starting to look a little bit better now. In the early days it looked like it was a foolish decision.

There was never going to be enough units produced to have any kind of economies of scale. Costs of the vehicles would be too big for the average Chinese person to afford. They switched their strategy a little bit. They brought in a different type of a car.

Most of the cars they're making now are midline cars that we would know in the States. They're sold to officials in the Chinese government.

A lot of U.S. auto parts suppliers who have done business with General Motors have been asked to go to China and either team up or whatever kind of an arrangement that they would like, to help support GM's operations in China. So, currently, the last two to three months, we're seeing better numbers come out of this new factory, and the future looks pretty bright.

So we would say it's a good start for U.S. auto manufacturers that are in -- in China. We're not looking at a major problem for those parts coming back into the U.S. We think this could be a start of a pretty substantial auto parts organization, joint ventures, alliances, whatever they may be, for Chinese manufacturers to take care of the domestic requirements of China.

It remains to be seen how it's going to work out, but at least that's how it's starting out. We're a big player in that area. And so far it's starting to work, but it's too early to really get a good picture of what the future may look like. But it's a good first step.

COMMISSIONER WESSEL: In terms of the plants that are there, the affiliations that your parts manufacturers have, what is the ownership? Is that -- I assume it's less than majority ownership; is that correct?

MR. CUTLER: In most cases it is less than majority ownership. Only a few that I'm familiar with that would be more than majority ownership.

COMMISSIONER WESSEL: And do you see servicing any part of the U.S. market out of those facilities, or is the consumption and demand great enough in China that you'll be simply producing for the markets there?

MR. CUTLER: We're hoping, and I think most other auto parts manufacturers are hoping, that the consumption requirement for domestic usage would be where most of the parts would go.

COMMISSIONER WESSEL: Thank you.

COMMISSIONER LEWIS: Thank you very much.
Any other questions from anybody?

Thank you so much for donating your time to educate us on these issues, and it was really a very helpful panel.

Thank you very much.

(Whereupon, the hearing recessed for lunch at 12:15 p.m. and went back on the record at 1:45 p.m.)

A-F-T-E-R-N-O-O-N S-E-S-S-I-O-N

(1:45 p.m.)

COMMISSIONER LEWIS: Okay. Let's start the afternoon session. Thank you very much for coming to attend our hearing. A great debate has been taking place in the United States about foreign trade and its impact on our country. The debate has involved elected representatives in Washington, economists, businesses that manufacture here, businesses that manufacture in foreign countries, exporters, importers, church leaders, union officials, environmentalists and think tanks. Foreign trade has been an increasing percentage of our gross national product, and with the passage of NAFTA and the defeat of fast track, the general public has become more aware of the issues.

Our Commission was created by Congress to study and report back on the causes and consequences of the U.S. trade deficit. We had technical briefings made to us in Washington to inform us of the nature of the issues involved, and we have been holding hearings around the country as mandated by the law of Congress that created us, on specific subjects. We've met in Pittsburgh, Palo Alto, and today in Seattle. We will also meet in Dallas, Washington, D.C., New York, and Kansas City. We have heard from people who have been helped by imports and from people who have been hurt by

exports.

There are those who laud the boom to some businesses and investors and consumers who credit foreign trade for these benefits and gains in some jobs, and we have heard from those who lament the loss of jobs, the inequality of income, and the bad things that have happened from foreign trade.

We've had two prior hearings -- in Pittsburgh and Palo Alto -- and two sessions this morning with people who have been informing us from both sides about the impact -- the causes and consequences of foreign trade.

We appreciate very much your being here. We would like each of you to take seven minutes to inform us what you're going to talk about. The green light will go on and then at five minutes it will switch to a yellow light, and then at the seven minutes -- red. I'll give you a two-minute warning. And then we'll have questions for each of you. We have a lot of time. So, I really appreciate your coming here.

Would Paul Isaki, who is a special -- State Special Trade Representative please be the first person?

Thank you.

MR. ISAKI: Thank you Mr. Chairman, members of the Commission. I'm pleased to be here today. My opening remarks will be brief. You have the more extended set of comments that I've submitted.

I think that the context that I'd like to speak to is essentially that the U.S. represents certainly one of the most open markets in the world from the standpoint of trade. By contrast, many of the companies in our state find difficult sledding in certain markets overseas because of both tariff and non-tariff barriers.

These barriers distort and restrict trade and U.S. exports and are a factor behind the deficit that you have been asked to examine.

Some of the examples of tariff and non-tariff barriers that I've cited in my extended remarks, and I'll simply mention it here, include tariffs on both agricultural and certain manufactured products. The policies behind tariffs -- to raise revenue from the tariff for the opposing country and also to provide a modicum of cushion to protect the domestic industry -- are not clearly the only reasons why tariffs are imposed, and their impacts differ.

It is difficult to imagine, for example, why certain countries levee a 40 percent tariff on imported frozen french fried products, a substantial